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BUDGET 2003

CONSULTATION PAPER

Introduction

On February 19, 2002 the provincial government tabled its 2002/03 budget which included a fiscal plan for the next three years (2002/03, 2003/04 and 2004/05). This consultation paper asks for your input on the government's next budget, which will extend the plan to include the 2005/06 fiscal year. The 2003/04 budget and an updated fiscal plan will be tabled on February 18, 2003.

Government's Three-Year Plan

The provincial government's priorities are to revitalize the economy, restore sound fiscal management and put patients and students first. The government's fiscal plan is key to delivering on these commitments.

The three-year fiscal plan set out a strategy to build a strong and vibrant provincial economy and balance the budget by 2004/05. The economic component of this strategy laid out four key elements:

- a competitive policy framework (for example: competitive tax rates, increased labour flexibility, streamlined regulations, elimination of business subsidies, and increased private sector participation in delivering infrastructure);
- agressive strategies to revitalize important sectors of our economy (for example: forestry, energy, mining, high-tech, tourism);
- sustainable environmental policies; and,
- educational excellence (for example, increasing high-tech graduates and expanding trades training).

In addition, the three-year fiscal plan detailed the financial spending targets necessary to achieve the legislated requirement to balance the budget by 2004/05:

- funding for health care was increased in 2002/03 and protected for 2003/04 and 2004/05. Education spending will be protected throughout the three-year plan;
- budgets of ministries except health care and education will be reduced by an overall 25 per cent over three years;
- as a result of the above, government spending will decline by 5 per cent overall.

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More information on the three-year fiscal plan is found in the *Budget and Fiscal Plan Summary — 2002/03 to 2004/05* at the end of this paper. The complete budget and three-year fiscal plan is available on the government web site at www.gov.bc.ca.

Recent Developments

In July, the final audited financial results for the last fiscal year (2001/02) showed a $1.23 billion deficit, a significant improvement from the $1.96 billion deficit forecast when this year's budget (2002/03) was introduced on February 19, 2002.

As well, a faster-than-expected economic recovery in B.C.'s North American trading partners has contributed to strong provincial economic growth in the first half of this year. As a consequence, the provincial economic outlook for 2002 has improved since the February 19 budget.

The government's finances have also improved slightly, despite the negative effects of the U.S. softwood lumber tariff. An updated financial forecast is included on *page v* of this consultation paper.

Budget Consultation

On February 18th of next year, as part of the 2003/04 budget, the provincial government will table a fiscal plan that extends the current three-year fiscal plan to 2005/06.

The government intends to maintain its overall spending targets and make only small changes to the fiscal plan for 2003/04 and 2004/05. The current forecast for the plan is a $4.0 billion deficit this year, a $1.7 billion deficit in 2003/04 and a balanced budget in 2004/05. If the government continues to be responsible in its spending decisions, economic growth can lead to higher government revenues in 2005/06. According to the current forecast, additional funds could be available on 2005/06 to:

- meet future needs in health care, education, economic development, or other program areas important to British Columbians;
- cut taxes to put more money in the pockets of British Columbians; or
- pay down the debt, reducing the burden on future generations of taxpayers, or
- some combination of the above choices.

Given the uncertainty of economic and financial forecasts, the government will also need to build in a forecast allowance or cushion at the start of each fiscal year, beginning in 2003/04, to provide greater assurance of meeting its budget targets. The forecast allowance provides a cushion to ensure the government achieves its financial forecasts and is also able to protect important social programs from unforeseen negative impacts like the fallout from September 11 last year.

In the coming months, the government will be deciding on these and other financial issues. To inform these decisions, the government is seeking British Columbian's views on the following three questions:

1. The government must maintain the overall spending targets set out in the current three-year fiscal plan that leads to a balanced budget in 2004/05. However, some changes to fine-tune the plan could be made in 2003/04 and 2004/05 by moving small amounts of money from one priority area to another. **If small changes were to be made, what should they be?**

2. After balancing the budget in 2004/05, revenue growth and continued spending control may provide additional funds in 2005/06. These funds could be allocated to priority programs (health care, education, economic development initiatives, etc), tax cuts, debt reduction or some combination of those options. **What should your government's fiscal priorities be for any available funds in 2005/06?**

3. **In what proportions would you allocate any available funds in 2005/06?**

The Legislature's Select Standing Committee on Finance and Government Services will hold public meetings in the province during September and October to seek the views of British Columbians on these issues. The committee will present its report to the Legislative Assembly by November 15, 2002. You can provide your views before October 25 by:

- appearing before the committee at one of its public meetings. The Committee's public meeting schedule is available on the legislative web site at www.legis.gov.bc.ca/cmt. Look for the Meeting Notices of the Select Standing Committee on Finance and Government Services;
- sending a written submission, letter or e-mail to the committee; or
- replying to the questionnaire on the next page.

You can also phone in toll-free 1-877-428-8337 or collect 1-250-356-2933.

To send your written submission, letter, e-mail or questionnaire to the committee, you can:

Mail to: Office of the Clerk of Committees
Room 224
Parliament Buildings
Victoria, British Columbia
V8V 1X4

Fax to: 1-250-356-8172 or

Email to: ClerkComm@leg.bc.ca

Questionnaire

1. Within the legislated requirement to balance the budget by 2004/05, my suggestions for fine-tuning the current three-year fiscal plan in 2003/04 and 2004/05 are:

2. My suggestions for using any available funds in 2005/06 are:

   A. Health Care:

   B. Education:

   C. Other spending areas (including economic development initiatives):

   D. Tax cuts:

   E. Debt Reduction:

   F. Other:

3. I would like to distribute any available funds in 2005/06 based on the following allocation:

Health	____ %
Education	____ %
Other spending	____ %
Tax cuts	____ %
Debt reduction	____ %
Must add up to	100%

Economic and Fiscal Forecasts
September, 2002

BC Economic Outlook	2002	2003	2004	2005
	---------- Annual per cent change ----------			
Real GDP	1.4	2.7	3.2	3.2

Financial Outlook	2002/03[1]	2003/04[1]	2004/05[1]	2005/06
	-------$ Millions unless otherwise noted-------			
Consolidated Revenue Fund				
Revenue	22,266	23,307	24,334	25,161
Spending				
Health care	(10,222)	(10,222)	(10,222)	(10,222)[2]
Education	(6,761)	(6,761)	(6,761)	(6,761)[2]
Other spending	(8,383)	(7,952)	(7,145)	(7,145)[2]
Total spending	(25,366)	(24,935)	(24,128)	(24,128)[2]
Crown Corporations	(165)	(53)	(13)	(33)
Expanded Entity[3]	—	—	(100)	(100)
Forecast allowance	(750)	Tbd[4]	Tbd[4]	Tbd[4]
Three-year fiscal plan				
Updated (deficit) surplus forecast	**(4,015)**	**(1,681)**	**93**	**balanced**
Funds potentially available in 2005/06 for targetted spending increases, tax cuts or paying down debt	**n.a.**	**n.a.**	**n.a.**	**900[2]**
Taxpayer supported capital spending	1,398	1,329	1,221	n.a.
Taxpayer supported debt	30,610	32,777	33,160	n.a.
Taxpayer-supported debt-to-GDP ratio	23.0%	23.6%	22.7%	n.a.

[1] Further details supporting the 2002/03 to 2004/05 forecasts are available in the *First Quarterly Report* for 2002/03. This and other budget and economic information can be found in the "Reports and Publications" section of the Ministry of Finance web site located at: www.gov.bc.ca/fin

[2] Assuming no expenditure or other policy change.

[3] The government passed legislation in 2001 to improve accounting transparency and to fully adopt generally accepted accounting principles by the 2004/05 fiscal year. This will more completely include the finances of schools, health authorities and advanced education organizations in the government's financial statements. The Ministry of Finance estimates these changes could increase costs by $100 million each year.

[4] To be determined at the start of each budget year.

Budget and Fiscal Plan Summary

2002/03 to 2004/05

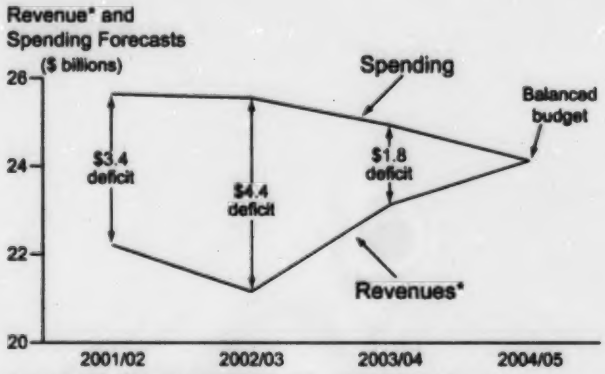
Issued
February 19, 2002

BRITISH COLUMBIA

Ministry of Finance

Summary

- A $4.4 billion deficit is forecast in 2002/03. The deficit is expected to decline to $1.8 billion in 2003/04, and a balanced budget is projected in 2004/05.



- The fiscal plan is based on the most likely economic revenue forecasts, with economic and revenue growth returning to more normal rates after weak economic performance in 2001 and 2002. The plan incorporates a revised forecast for 2001/02, updates to the three-year ministry spending plans announced on January 17, 2002 and Crown corporation financial forecasts.

- The $4.4 billion deficit for 2002/03 results from a $815-million decline in revenues, a $81-million decrease in spending, a $442-million improvement in Crown corporation contributions, and a $750-million forecast allowance as a cushion against potential risks to the budget.

- No forecast allowances are included in 2003/04 or 2004/05 at this time. However, to help the government meets its financial targets, appropriate allowances will be determined when budgets for each of those years are presented.

- After 2002/03, revenues are forecast to grow an average of 5.1 per cent annually, in line with the 4.6-per-cent average growth in nominal GDP. Spending will decline by an average of 2.8 per cent annually. The resulting $2.3 billion revenue increase and $1.4 billion spending decrease, combine to reduce the deficit to zero by 2004/05.

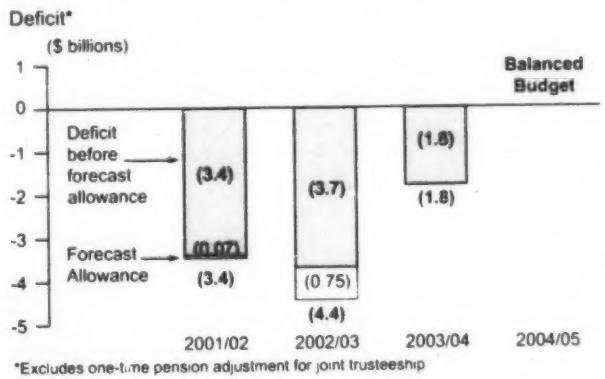
- The revised forecast deficit for 2001/02 is $3.4 billion excluding the one-time pension adjustment, and includes a $70-million forecast allowance. The deficit forecast is consistent with the second *Quarterly Report* released on November 22, 2001.

Fiscal Plan

- The fiscal plan is presented on a three-year basis. Forecasts and plans for revenues, ministry spending and Crown corporations are provided for each of the three fiscal years 2002/03, 2003/04 and 2004/05. Accompanying service plans for ministries and Crown corporations detail expected changes, accomplishments, and performance targets. The government is also releasing a three-year strategic plan along with the budget and service plans.

- After the end of each fiscal year, results will be reported in the *Public Accounts*, a report on government strategic plan results, and ministry and Crown corporation service plan reports. Every year, these plans will be reviewed and updated to reflect progress made and changing economic and financial circumstances, and another year will be added. The *Quarterly Reports* will include regular updates on any significant changes and policy developments occurring within each year.

- Starting April 1, 2002, Cabinet ministers are collectively and individually accountable for spending control and will incur salary penalties for failure to stay within budget or meet specified performance targets. All ministers are collectively responsible for meeting the overall deficit target of $4.4 billion. As for individual responsibility, some ministers must focus on not overspending their ministry 2002/03 authorizations, while the Minister of Provincial Revenue and Ministers of State must focus on achieving specific performance results.



*Excludes one-time pension adjustment for joint trusteeship

- The three-year fiscal plan is based on two main strategic elements:

  — building a strong and vibrant economy; and

  — eliminating the deficit.

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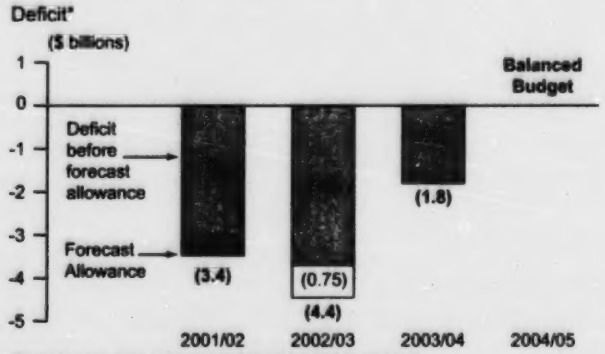

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  — building a strong and vibrant economy; and

  — eliminating the deficit.

Building a Strong and Vibrant Economy

Government's overall strategy for restoring confidence in the economy and creating a stable, growing revenue base has four key elements.

1. A stable and competitive policy framework:

- The personal income tax cuts announced on June 6, 2001, business tax cuts, and other measures announced with the July 30 *Economic and Fiscal Update*, are major steps towards the goal of restoring economic competitiveness.
- The government intends to review the tax system on a regular basis to ensure it remains competitive with other jurisdictions.
- This budget includes several tax measures to further improve the competitive environment, including expanding the definition of parts that are exempt from provincial sales tax and raising the small business corporate income tax threshold.
- The private sector will play a greater role in providing public infrastructure and services through the use of public-private sector partnerships.
- The *Employment Standards Act*, the *Workers Compensation Act* and the Labour Code will be updated to improve flexibility and to ensure they are fair to employers and employees alike.
- Government is also taking steps to reduce the regulatory burden and level the playing field for investment by eliminating business subsidies.

2. Ambitious but achievable sector strategies:

- The government is taking steps to:
  - — revitalize BC's forest industry;
  - — maximize development opportunities in BC's energy sector;
  - — work with industry to double tourism's contribution to the province's economy, including aggressive support for British Columbia's bid to host the 2010 Olympic Winter Games;
  - — encourage mineral exploration and development;
  - — ensure that British Columbia becomes a global leader in high-tech;
  - — encourage other sectors including agriculture and aquaculture as well as film and television production; and
  - — encourage the vital small business sector by removing barriers to growth and exploring opportunities for expansion.

3. Sustainable environmental policies:

- The government places a high priority on a thriving private sector that also respects British Columbians' strong environmental values.
- To ensure the benefits enjoyed today are available to future generations, the government will respect the following principles:
  - — setting appropriate environmental standards and creating incentives to meeting those standards;
  - — managing British Columbia's natural resources on a sustainable basis;
  - — minimizing land-use conflicts through co-ordinated decision-making;
  - — basing decisions on the best available scientific knowledge; and
  - — working in partnership with all levels of government to harmonize standards and establish clear accountability for results.

4. Educational excellence:

- BC's economic prosperity will depend on a high quality, relevant education system that equips students with the skills and knowledge they need. Key initiatives to achieve this goal include:
  - — increasing the number of high-tech graduates, particularly in computer science and electrical and computer engineering;
  - — expanding industry training in areas such as general trades training and new apprenticeships;
  - — forging closer links between education and the economy through professional interchanges and leading edge research chairs; and
  - — creating more choice for students through enhanced on-line learning and expanded transferability of credits between institutions.

Eliminating the Deficit

- On January 17, 2002, the government announced three-year spending plans that reduced funding for ministries, except Health Services, Education and Advanced Education, by a total of 25 per cent or $1.9 billion over three years.
- Within the fiscal framework provided by current economic, revenue and Crown corporation forecasts, the spending reductions are forecast to contribute to achieving a balanced budget in 2004/05. Compared to the July 30 *Economic and Fiscal Update*, total spending in 2004/05 will fall by $974 million.
- In 2002/03, the $4.4-billion deficit forecast takes into account:
  - — an underlying structural deficit;
  - — weak revenues reflecting the economic slowdown and lower commodity prices;
  - — the ongoing investment in personal and business tax cuts announced last year;
  - — one-time costs associated with the restructuring of government;
  - — the first phase of the three-year spending cuts; and
  - — a $750-million forecast allowance to protect against economic risks and resulting revenue shortfalls.
- The government is also faced in 2002/03 with almost $800 million in compensation costs associated with recruiting and retaining high-demand health care workers and professionals, including doctors. To offset these additional health care costs, the government is raising Medical Service Plan premiums, increasing the sales tax rate by one-half a percentage point, and increasing taxes on tobacco.
- The revenues, expenditures and Crown corporation contributions for each year of the three-year fiscal plan are outlined below:

Three-year Fiscal Plan	Revised Forecast[1] 2001/02	Plan 2003/04	Plan 2004/05
		(millions)	
Consolidated revenue fund (CRF):			
Revenue	22,853	23,159	24,325
Expenditure	(25,637)	(24,935)	(24,128)
CRF balance	(2,784)	(1,776)	197
Total net contributions (loss) of Crown corporations and agencies	(574)	(24)	(97)
Subtotal	(3,358)	(1,800)	100
Expanded government entity	—	—	(100)
Forecast allowance	(70)	—	—
Deficit before joint trusteeship	(3,428)	(1,800)	—
Joint trusteeship (one-time adjustment)	1,464	—	—
Deficit	(1,964)	(1,800)	—

[1] Restated to be consistent with the presentation used for 2002/03.

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CRF balance	(2,784)	**(3,518)**	(1,776)	197
Total net contributions (loss) of Crown corporations and agencies	(574)	**(132)**	(24)	(97)
Subtotal	(3,358)	**(3,650)**	(1,800)	100
Expanded government entity	—	**—**	—	(100)
Forecast allowance	(70)	**(750)**	—	—
Deficit before joint trusteeship	(3,428)	**(4,400)**	(1,800)	—
Joint trusteeship (one-time adjustment)	1,464	**—**	—	—
Deficit	(1,964)	**(4,400)**	(1,800)	—

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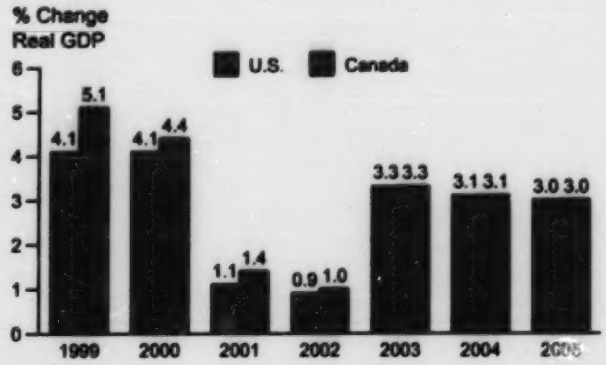
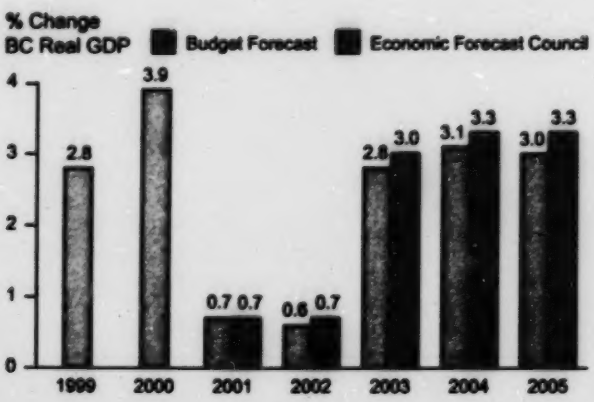
Economic Outlook

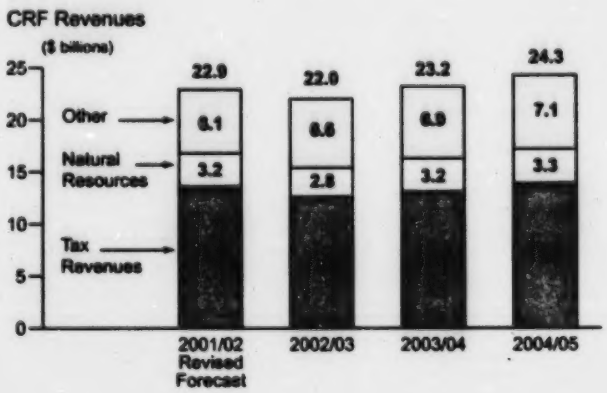


- The U.S. economy is expected to recover in 2002 and the Canadian economy is expected to follow. In 2003 and beyond, the U.S. and Canadian economies are expected to lead global economic growth.
- Based on these assumptions of growth in the province's major markets and other external assumptions, the British Columbia economy is forecast to grow 0.6 per cent in 2002, and then pick up to 2.8 per cent growth in 2003.
- The average forecast of the British Columbia Economic Forecast Council is slightly higher, with expected growth of 0.7 per cent in 2002 and 3.0 per cent in 2003.
- In 2004 and 2005, the British Columbia economy is forecast to grow about 3.0 per cent each year, consistent with the outlook for the province's trading partners, firmer commodity prices and stronger consumer and business sectors.
- Investment in the province is forecast to pick up by 2003 reflecting an improved business outlook as well as the medium-term impact of a more competitive tax environment.
- The main risks to the economic outlook include higher or lower-than-expected growth in the Canadian and U.S. economies, and the outcome of the softwood lumber dispute.



Revenues

- Revenues are expected to decline by $815 million in 2002/03 reflecting:
  - — the impact of tax cuts announced on June 6 and July 30, 2001, which further reduce revenues by $755 million;
  - — further tax competitiveness measures worth roughly $25 million;
  - — a decline in corporate income tax revenues reflecting the effect of weak corporate profits in 2001;
  - — various one-time income tax revenue increases occurring in 2001/02 that will not occur in 2002/03; and
  - — new revenue measures totalling $758 million to pay for health care system compensation costs. After factoring in tax competitiveness and other measures, total revenue measures in 2002/03 are reduced to $736 million.
- After declining by 3.6 per cent in 2002/03, revenues are expected to increase at an average rate of 5.1 per cent from 2002/03 to 2004/05. This reflects the global economic recovery and firming commodity prices.



Crown Corporations

- Crown corporations turned in a weaker-than-expected performance in 2001/02, mainly reflecting restructuring by BC Rail, higher costs at ICBC along with a writedown of the Surrey City Centre development, and lower-than-expected results from BC Hydro. Crown corporation finances are forecast to show a modest improvement between 2002/03 and 2004/05, mainly due to improving results for ICBC, BC Rail and BC Lotteries.
- The government is still continuing its core reviews of Crown corporations. As well, there are a number of other initiatives, such as the Energy Policy Review, that could affect the future of Crown corporation activities. As these reviews are completed, Crown corporation service plans will be updated to reflect new directions.

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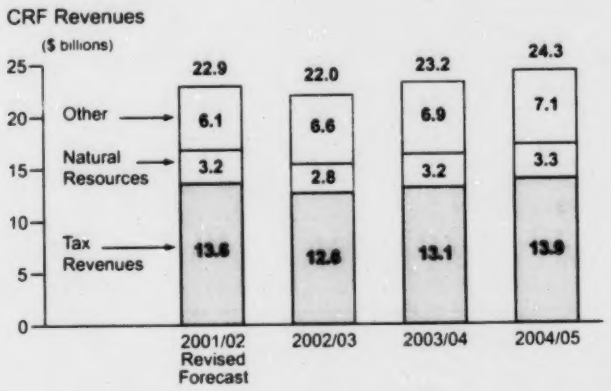

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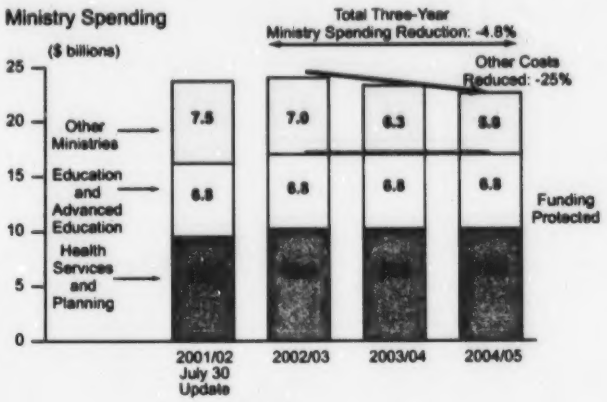
Revenue Measures

- The revenue measures included in *Budget 2002* are designed to:
  - — raise additional revenue to pay for compensation increases in the health sector to ensure the retention and recruitment of high-demand health workers and professionals; and
  - — continue with changes to make the tax system more competitive.
- These changes combined with recently announced flexibility measures will help to offset additional health sector compensation costs totalling almost $800 million in 2002/03:
  - — a 50 per-cent increase in MSP premiums that will raise $358 million in 2002/03. Enhancements to the premium assistance program ensure that premiums will be reduced or eliminated entirely for 230,000 lower income British Columbians;
  - — raising the provincial sales tax rate to 7.5 per cent from 7 per cent. This will raise $250 million in 2002/03. The refundable sales tax credit will be increased by $25 to $75 per adult to protect lower income taxpayers that currently receive the credit; and
  - — increasing the tobacco tax rate by $8 per carton of 200 cigarettes, and the tax on fine-cut tobacco by an equivalent amount. After taking into account changes in smoker behaviour, this is expected to raise $150 million in 2002/03.
- To build on the process of improving British Columbia's tax competitiveness, the definition of parts that can be purchased exempt from provincial sales tax is expanded and the threshold for the small business income tax rate will be increased to $300,000 from $200,000. These measures will return roughly $25 million to small business taxpayers in 2002/03.
- *Budget 2002* also fulfills the New Era commitment to refund provincial sales tax on purchases for schools made with parent advisory council raised funds.

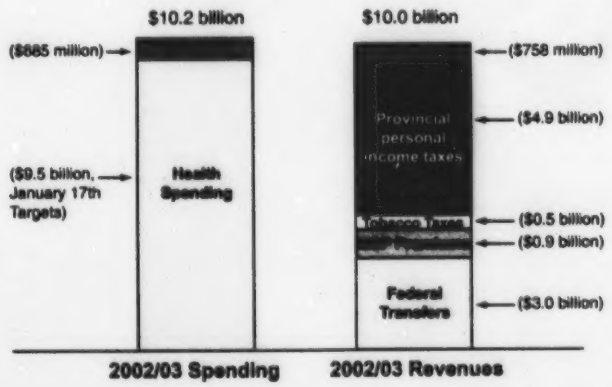
Spending Plan

A) Operating Spending

- For 2002/03, total government spending, which includes ministry spending, debt interest costs, other appropriations and an expenditure contingency reserve, is budgeted at $25.6 billion.
- Total ministry spending of $24.0 billion includes $23.3 billion as announced with government's three-year spending targets on January 17, 2002, and additional health care funding of $685 million. A further $73 million has been included in the Contingencies (All Ministries) and New Programs Vote for health compensation costs.
- While total ministry spending will fall 4.8 per cent by 2004/05, funding for health and education has been protected.
- Spending in the ministries outside the health and education areas will decline by $1.9 billion (25 per cent) over the next three years.



- When debt interest, restructuring and special offices costs are included, overall government spending will fall 3.9 per cent by 2004/05.



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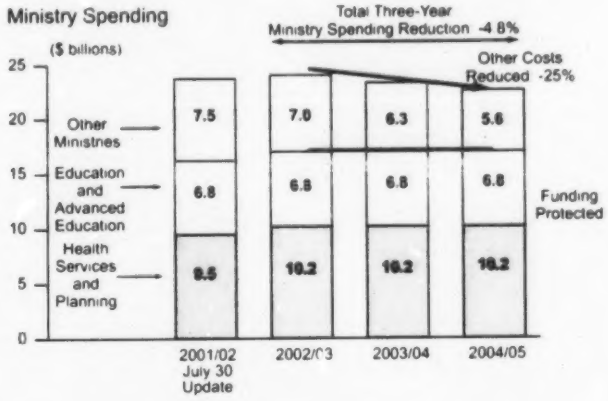
Spending Plan

A) Operating Spending

- For 2002/03, total government spending, which includes ministry spending, debt interest costs, other appropriations and an expenditure contingency reserve, is budgeted at $25.6 billion.
- Total ministry spending of $24.0 billion includes $23.3 billion as announced with government's three-year spending targets on January 17, 2002, and additional health care funding of $685 million. A further $73 million has been included in the Contingencies (All Ministries) and New Programs Vote for health compensation costs.
- While total ministry spending will fall 4.8 per cent by 2004/05, funding for health and education has been protected.
- Spending in the ministries outside the health and education areas will decline by $1.9 billion (25 per cent) over the next three years.



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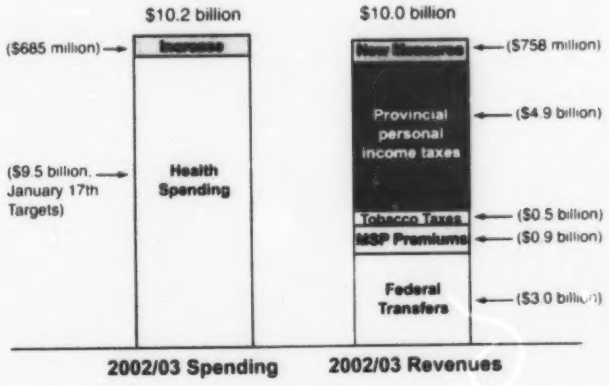


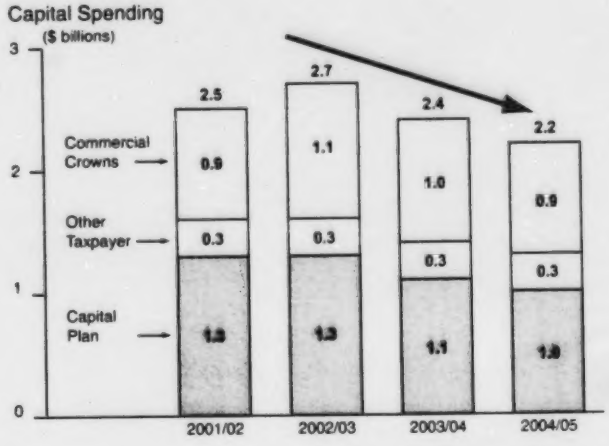
- Due to increased compensation costs associated with recruiting and retaining high-demand health care workers and professionals, $685 million has been added to the health budget for

2002/03 and $73 million to the contingencies vote. This includes the costs to fund the 21-per-cent increase in nurses' salaries, the health science workers' agreement and the February 8, 2002 interim arbitration award for doctors. Overall health spending rises from $9.5 billion in the July 30 Update to $10.2 billion today, a 7.1 per cent increase.

- The total expected revenues for this year from all federal transfers, Medical Services Plan premiums, personal income taxes and the new revenue measures — which increase Medical Service Plan premiums, social services tax and tobacco taxes by a total $758 million — still do not equal the total health budget. For 2002/03 the health budgets account for 40 per cent of CRF spending and 46 per cent of CRF revenues.

B) Capital Spending

- The government is introducing two changes in the way capital budgets are developed:
  - — capital funds are no longer allocated through a separate budgeting process. Instead, operating and capital budgeting decisions have been integrated and are driven by service plan objectives, constrained by the limits of ministry operating budgets. Ministries must ensure they have sufficient funds to cover all operating and maintenance requirements, as well as amortization and debt interest costs associated with capital facilities; and
  - — recognizing their budget limitations, ministries and agencies are being challenged to explore new ways of funding and managing capital projects. The focus will be on effective and efficient delivery of public services, while infrastructure ownership and direct control will become subordinate issues.



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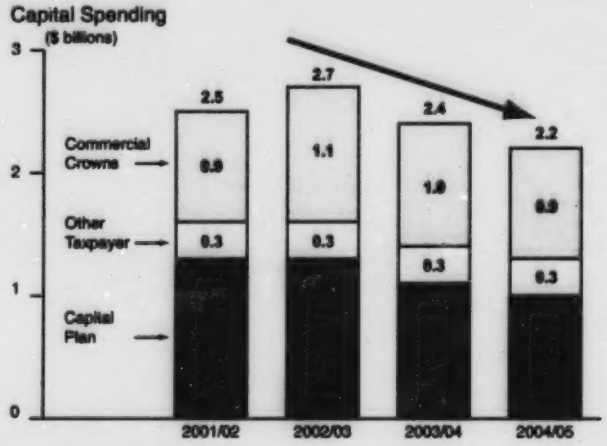

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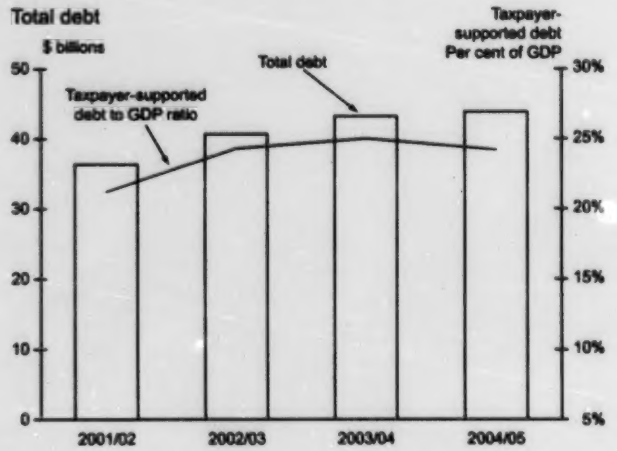
Managing Risks to the Fiscal Plan

- To manage potential risks and to help ensure the achievement of the targeted deficit, a forecast allowance of $750 million — over three per cent of revenues — is included in the 2002/03 budget. This forecast allowance increases the expected deficit from government's most likely forecast of $3.65 billion to a more conservative forecast of $4.4 billion.
- In addition, ongoing monitoring and updating of the revenue and expenditure outlook will provide the ability to take early corrective action.
- Over the next two years, government will take further action as necessary and will incorporate annual forecast allowances into the 2003/04 and 2004/05 budgets based on an evaluation of the risks faced at that time. This will provide greater assurance of achieving annual fiscal targets, and meeting the legislated requirement to balance the budget beginning in 2004/05.

Debt

- Total government debt is expected to increase from $36.4 billion to $43.9 billion over the next three years primarily reflecting cumulative deficits and capital spending. However as the deficit is reduced to zero, the rate of debt increase will slow, and the taxpayer-supported debt-to-GDP ratio is forecast to start to decline in 2004/05.



- The increase in total debt underscores the importance of eliminating the deficit as quickly as possible, to avoid burdening future generations of British Columbians with rapidly escalating debt interest costs.
- The eventual decline in the taxpayer-supported debt-to-GDP ratio, a key measure of the province's ability to repay debt, reflects the importance of both strong economic growth and balanced budgets in achieving an affordable level of debt.
- This budget sets out a plan to build a strong and vibrant economy and to eliminate the deficit, thereby restoring confidence in the future. The plan puts the province's finances on a sound, sustainable path and returns prosperity to British Columbians.